No. 84-16

# In the Supreme Court

OF THE

# United States

October Term, 1984

Kenneth Cory, Leo T. McCarthy,
and Jesse R. Huff,
members of the California State Lands Commission,
*Appellants,*
vs.
Western Oil & Gas Association, et al.,
*Appellees.*

**On Appeal from the United States Court of Appeals for the Ninth Circuit**

## BRIEF FOR THE APPELLEES

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## QUESTION PRESENTED

Whether a state bordering on the ocean, owning 93% of tide and submerged land (and, together with its local political instrumentalities, owning all available such land) may collect the equivalent of a tariff on goods exported to or imported from abroad and to and from other states by charging a throughput rental for crossing of tide and submerged lands. A throughput rental means a charge for each barrel (or other measure) of cargo crossing leased state tide or submerged land.[1]

## PARTIES BELOW

Appellants are as described in their brief. Appellees include, in addition to those described in appellants' brief, Edgington Oil Company.

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[1] This case does not involve the validity of such a charge on other than tide or submerged lands. Appellants' brief states the question much too generally.

## TABLE OF CONTENTS

TABLE OF CONTENTS

## TABLE OF AUTHORITIES CITED

### Cases

Page

## Table of Authorities Cited

### Cases

## Table of Authorities Cited

### Cases



### Constitutional Provisions, Statutes, and Regulations

TABLE OF AUTHORITIES CITED

CONSTITUTIONAL PROVISIONS, STATUTES, AND REGULATIONS



**Miscellaneous**

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## BRIEF FOR THE APPELLEES

### OPINIONS BELOW

The opinions below are those referred to by appellants in their brief.

### JURISDICTION

The basis for jurisdiction is as set forth by appellants in their brief.

### CONSTITUTIONAL PROVISIONS, STATUTE, AND REGULATIONS INVOLVED

1. The Commerce Clause, the Import-Export Clause, and the Tonnage Clause of the United States Constitution are as set forth by appellants, as is the challenged provision for a "throughput" charge.

2. In addition, the provisions of Section 3 of the Submerged Lands Act, 43 U.S.C. § 1311, are as follows:

> "(a) It is determined and declared to be in the public interest that
>
> (1) title to and ownership of the lands beneath navigable waters within the bounderies of the respective States, and the natural resources within such lands and waters, and
>
> (2) the right and power to manage, administer, lease, develop, and use the said lands and natural resources all in accordance with applicable State law be, and they are subject to the provisions hereof, recognized, confirmed, established, and vested in and assigned to the respective States or the persons who were on June 5, 1950, entitled thereto under the law of the respective States in which the land is located, and the respective grantees, lessees, or successors in interest thereof;
>
> (b) (1) The United States releases and relinquishes unto said States and persons aforesaid, except as otherwise reserved herein, all right, title, and interest of the United States, if any it has, in and to all said lands, improvements, and natural resources."

3. Article X of the California Constitution provides as follows:

§ 3. *Tidelands, Withholding From Grant or Sale.*

All tidelands within two miles of any incorporated city, city and county, or town in this State, and fronting on the water of any harbor, estuary, bay, or inlet used for the purposes of navigation, shall be withheld from grant or sale to private persons, partnerships, or corporations; provided, however, that

any such tidelands, reserved to the State solely for street purposes, which the Legislature finds and declares are not used for navigation purposes and are not necessary for such purposes may be sold to any town, city, county, city and county, municipal corporations, private persons, partnerships or corporations subject to such conditions as the Legislature determines are necessary to be imposed in connection with any such sales in order to protect the public interest.

§ 4. *Access to navigable waters.*

No individual, partnership, or corporation, claiming or possessing the frontage or tidal lands of a harbor, bay, inlet, estuary, or other navigable water in this State, shall be permitted to exclude the right of way to such water whenever it is required for any public purpose, nor to destroy or obstruct the free navigation of such water; and the Legislature shall enact such laws as will give the most liberal construction to this provision, so that access to the navigable waters of this State shall be always attainable for the people thereof.

## STATEMENT OF THE CASE

### A. The Basic Controversy.

This case concerns the imposition of a charge on lessee importers or exporters of petroleum for crossing state tide and submerged lands. From the inception of the Constitution, it has been recognized that the States owned the land beneath the harbors and other navigable waters within their borders. *United States v. California*, 332 U.S. 19, 31 (1947), acknowledges as much. That decision denied the States such a title along the coast out to the three-mile limit. But in 1953, Congress adopted the

Submerged Lands Act, conveying to the states title to all land underlying the harbors and seas of the United States from the mean high tide mark to the three-mile limit. 43 U.S.C. § 1301, *et seq.* Congress thus surrounded the United States with a band of real property, the legal title to which rested in the states rather than the federal government. Use of the submerged land obtained from these two sources is essential for all maritime and a great deal of pipeline commerce. Every dock must be placed upon the tidelands; every pipeline connection to every offshore well must be placed upon those tidelands. Virtually every anchorage where every tanker or ship comes to rest is within that band of property. The State (or its creations, cities to whom it has granted such property) has physical control over all such properties. No docks, no pipelines, none of the facilities which are essential to maritime commerce can be constructed without the consent of the State or its instrumentalities. The State itself owns more than 93% of all tide and submerged lands and, with its instrumentalities, virtually 100% (*See* discussion *infra*, pp. 26-27). Although appellants now urge the contrary, both the District Court and the Court of Appeals found that plaintiffs *must* use State lands. (J.S.App. A-2, 17-18.)

The question presented here is whether the State may use this control to impose what amounts to a duty or tariff on goods imported by sea into the State. As will be shortly demonstrated, the State has adopted regulations allowing it to collect as rental what it calls a "throughput rental"; *i.e.*, a charge for every barrel of petroleum and other merchandise which crosses this band of real estate, using as a foundation its power to require a lease for the construction of the dock or pipeline required to bring such crude oil into the state. In our view, that charge is not different from a straightforward tariff. It is measured in the same way; it is paid by the same people; the

governing event is the same. Nonetheless, the State justifies it, essentially on the premise that as owner of the tidelands, it can charge whatever "rental" it wishes.

**B. Position of The Parties.**

Appellants are the members of the California State Lands Commission. They are the state officials who adopted and consequently enforced the challenged regulation.

Appellees are the Western Oil and Gas Association and certain of its members (hereafter "WOGA" or "lessees"). WOGA is a trade association comprising most of the individual companies in the oil business who are affected by the rule we challenge. These are companies engaged in the transportation in foreign and interstate commerce of petroleum and petroleum products which must traverse the State's tidelands, its sea border. They have constructed facilities of great value in part upon tidelands and in part on adjoining real estate. Those facilities include refineries, wharves, mooring facilities, petroleum-producing platforms and oil and gas pipelines. (J.A. 19-20, 52-3, 59-60, 73-4, 89-90.) Utilization of these facilities is indispensable to the interstate and foreign flow of crude oil, gas and petroleum-derived products.[2] In turn, because of their location, the State's lands are indispensable to the use of the facilities for such commerce.[3]

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[2]For example, about 95% of the crude oil which passes over the State's land into Chevron's Richmond refinery moves in interstate or foreign commerce (J.A. 61); 100% of Shell's crude is interstate or foreign (J.A. 75); 100% of Union Oil's (J.A. 22).

[3]Based on the lessees' declarations, both the District Court and the Court of Appeals found:

> "Plaintiffs own several oil and gas processing plants located on or near the coast of California. The amount of capital invested

## C. History of the Regulations.

Prior to 1976, the State Lands Commission's (hereafter "SLC" or "Commission") practice was to appraise the land used by a dock, pipeline or other facility and fix a rental at the percentage which constituted the going market rental for property of that value. The reasonableness of that approach is not challenged: a person who has the exclusive use of a piece of the State's property should pay a fair rental for it, and that method undoubtedly provides for such a rental. Because the fair market value did not exploit for the State the full value of its strategic position, the Commission determined to collect, in addition, a thoughput charge; *i.e.,* a charge based on the volume of commodities crossing the leased land.

The proposed regulations were the subject of several days of hearings. The testimony offered was without exception that the effect of such a system of charges would be to discourage commerce. (See, *e.g.,* J.A. 162-244.)

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in these facilities is substantial. Petroleum substances must enter or depart from these facilities through a system of pipelines. Due to the physical and practical immobility of plaintiffs' processing plants, the pipelines *must traverse tidal and submerged lands owned by the State.* Up to ninety-five percent (95%) of the petroleum substances entering the facilities are of foreign origin. Some forty-six to ninety-eight percent (46-98%) of the petroleum products leaving the facilities are channeled into interstate and foreign commerce. These products remain in such commerce until they reach the ultimate consumer. *See, e.g., Maryland v. Louisiana,* 101 S.Ct. 2114, 2134 (1981)."

(J.S.App A-17-18; *see* J.S.App. A-2, 5 (emphasis added).)

That finding by the two courts below is now firmly established. *Branti v. Finkel,* 445 U.S. 507, 513 (1980), *Pick Mfg. Co. v. General Motors Corp.,* 299 U.S. 3, 4 (1936). The factual basis for such a finding will not be reviewed by this Court. (*Ibid.*)

The Commission attempted to make a record justifying the proposal on the basis that similar charges are made by cities which have received conveyances of tidelands from the State and which operate ports. The record actually is, however, that such rates are not at all comparable. (J.A. 183-4, 413-420.) Ports provide valuable services and facilities, such as dredging, navigation aids and breakwaters. (J.A. 389-450.) In contrast, the SLC provides unimproved land. It does no dredging, provides no navigational aids, breakwaters or other facilities. (J.S.App. A-9-10, 18.)

The Administrative Record contains one report which specifically analyzes the tariffs charged by port authorities for use of their land and facilities. This report, entitled "Final Report and Cost Formula for the California Association of Port Authorities," flatly disproves the SLC's contention that port authorities employ volumetric tariffs which are not based upon a reasonable return on the appraised value of port land and improvements. It states, on the contrary, that ports generally charge on a basis akin to a public utility rate, *i.e.,* on a basis calculated to produce a reasonable return on the investment. (J.A. 400-420.) Finally, the one report in the Administrative Record concerning a fair rental for the SLC's land — the Clark Report commissioned by the SLC itself — recommended a flat eight percent rental. The Report stated that rental formats other than appraisal and percentage were inapplicable to leases of industrial land. (J.A. 324.)

Nevertheless, on April 28, 1976, the SLC amended its regulations for the leasing of all tidelands and submerged lands owned by the State. The regulations were codified in 2 California Administrative Code § 2005 (now § 2003), as follows:

"2005. *Payment of Rentals.*

"(a) . . . .

"(b) Rental Rate Schedule: The following rates shall apply to the classifications listed below:

. . . .

"(2) *Industrial Use:* The rental may be based on eight percent (8%) [now 9%] per annum of the appraised value of leased land together with 1.5 [now 2] cents per diameter inch per lineal foot for pipelines and conduits within the leased premises; and/or *an annual rental, with a specified minimum, based upon the volume of commodities passing over State land*. The minimum rental under either of these alternative rentals shall not be less than $550 per annum."

"(3) *Right of Way Use.* Eight percent (8%) [now 9%] per annum of the appraised land value, together with damages, if any; and/or for pipelines and conduits, 1.5 [now 2] cents per diameter inch per lineal foot per annum, or, in lieu of either of the foregoing, *an annual rental, with a specified minimum based upon the volume of commodities passing over State land.* The minimum rental under any of the above alternatives shall not be less than $100 per annum."

(Emphasis added.)

The italicized portions of these regulations provide for the throughput charge.

**D. Application of the Rule.**

The rule adopted by the State Lands Commission did not provide for a *fixed* throughput charge. It left the amount of the throughput charge to be "negotiated" separately in each lease made by the State, thus placing the State in the position to charge the maximum that the

traffic would bear. The history of such "negotiations" is as follows:

At the time this action was first brought in federal court, the SLC had already entered into one lease which imposed a throughput charge on the lessee. That lease set the procedural pattern for others to come. In each instance since the regulations were adopted, the SLC has appraised the leased land and has set a minimum rental of eight percent of the appraised value of that leased land. (Today, with the general rise in interest rates, that charge is nine percent.) This method is consistent with that used under the SLC's prior regulations to compute total annual rentals. The Commission, however, has gone on to impose an additional levy based on the volume of commodities passing over the lands being leased. In each such instance, the additional charges have resulted in payments substantially in excess of the fair rental value.

Pacific Refining Company ("Pacific") was the first company to be required to make rental payments, albeit under protest, pursuant to the SLC's throughput regulations. In April of 1976, Pacific purchased a refinery at Hercules, California, from Gulf Oil Corporation ("Gulf") (J.A. 53). As part of the transaction, Gulf agreed to assign its lease rights to Pacific. *(Ibid.)* Consent of the SLC is required before such an assignment can become effective, and that consent was sought by the parties. *(Ibid.)*

During negotiations, the SLC took the position that it would not consent to an assignment unless the lease was amended to include a throughput provision. (J.A. 53-4.) Faced with this predicament, Pacific executed an amendment to its lease containing a throughput provision. (J.A. 53.) All of Pacific's crude is imported (J.A. 54-5.)

At an eight percent annual return, which was then found to be fair market value, Pacific would pay the SLC

$32,500 each year. When a throughput charge was added, for the first few years the charge amounted to an annual rate of return on unimproved state land of 28 to 29 percent of the appraised value of the land. (J.A. 54.)

Other companies faced similar dramatic increases in lease charges. Union Oil Company of California, with a refinery investment of almost 200 million dollars and the vast majority of commodities passing through its pipelines in either interstate or foreign commerce, has been forced to pay an annual net rate of return for its ten-year lease of SLC land of approximately 18 percent for each of the first five years and 23 percent annually for each of the next five years. (J.A. 21.) Chevron U.S.A. Inc., with a refinery investment of over $723,000,000 and approximately 95 percent of the commodities passing through its pipelines in interstate or foreign commerce, pays an average net rate of return from 1977 through 1986 of approximately 21.5 percent each year, with a high return for 1984, 1985 and 1986 of over 24 percent a year. (J.A. 60-61.)

One final example is provided by Shell Oil Company, whose wharf connects to its Martinez manufacturing complex. One hundred percent of its crude oil transported over the wharf is in interstate or foreign commerce. (J.A. 75.) The throughput charge results in an *average* annual net rate of return of 17.57 percent, which approximately doubles the rent. *(Ibid.)*

## ARGUMENT

### I

### Preliminary

Throughout this case, we have rested our arguments on a few basic propositions. The State has never chosen directly to address any of them. They are as follows:

1. The State may without doubt, subject companies in interstate or foreign commerce to a considerable variety of taxation uniformly applicable to all business within the state. But it is equally without doubt that under the Constitution no state or state instrumentality may impose a tariff on goods for the simple privilege of entering the state, whether the tariff be one on goods traveling in interstate commerce or goods in foreign commerce.

This principle is not of recent origin. Indeed, the proliferation of local tariffs under the Articles of Confederation was the principal cause for the calling of the Philadelphia Convention which wrote the Constitution. The principle continues to have current significance; economic balkanization has not come to be more attractive with the passage of time.

2. From the days of the Articles of Confederation, the land beneath the harbors has belonged to the State. *(See United States v. California,* 332 U.S. 19, 31 (1947).) In addition, in 1953, by the Submerged Lands Act (43 USC § 1301 *et seq.*), Congress granted to the states coastal tide and submerged land from the mean high tideline out to the three-mile limit. These tide and submerged lands are the lands on which both docks and pipelines to and from vessels or outer Continental Shelf installations have to be built. The State by itself has 93% of such lands: with its political subdivisions it has essentially all. It is impossible to land commodities so transported, whether solid or liquid, without utilizing the lands thus held by the states or their instrumentalities, the cities. If the State can collect a volumetric charge based simply on the amount of a commodity which crosses tide and submerged acreage — as "rental" for the use of that land (without reference

to any other service performed) — then it can collect an amount which differs in no respect from a tariff. But California cannot be permitted to rely on a "rental" formula that exploits its control over the crucial tidelands. "[A]s it cannot be done directly, it could hardly be a just and sound construction of the Constitution which would enable a State to accomplish precisely the same thing under another name, and in a different form" *License Cases*, 46 U.S. (5 How.) 504, 576 (1847).

3. The State has made no claim that it is free to collect a tariff. And up to this moment, the State has not sought to demonstrate that there is so much as a nickel's difference between a tariff, a tax, or a "throughput rental" placed on every barrel of petroleum brought into the state. It has, rather, sought to establish the proposition that so long as the charge is designated "rent," and perhaps so long as it resembles some charge sometimes collected by private lessors, the State can charge anything it wants. Those propositions are invalid. Although the volumetric rates are designated as "rent" by the State, it is the practical effect of an exaction, not its label that is the focus of analysis under the Commerce Clause. *See, e.g., Commonwealth Edison Co. v. Montana*, 453 U.S. 609, 615 (1981); *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274, 279 (1977); *Nippert v. Richmond*, 327 U.S. 416, 431 (1946).

Since the State does not seriously contend that its charges could be justified as a tax, our discussion of principles applicable to taxation will be brief. But because the principles involved are vital, we will start with them.

## II

## The Constitution Denies to the States the Power to Collect a Charge on Goods for Entry into the State.

The limitations on State power with which we are concerned here are no recent invention. They have their origins in the very formation of the Constitution. It is a familiar fact of history that in the days of the Articles of Confederation the states levied an array of duties and protective tariffs, both on imports from abroad and from other states.

> "Finance, commerce, and business assembled the historic Philadelphia Convention; although it must be said that statesmanship guided its turbulent councils. The senseless and selfish nagging at trade in which the States indulged, after peace was declared, produced a brood of civil [abuses.] The States passed tariff laws against one another as well as against foreign nations; and, indeed, as far as commerce was concerned, each State treated the others as foreign nations. There were retaliations, discriminations, and every manner of trade restrictions and impediments which local ingenuity and selfishness could devise.
>
> The idea of each State was to keep money from going outside its borders into other States and to build up its own business and prosperity at the expense of its neighbors. States having no seaports were in a particularly hard case. Madison picturesquely describes their unhappy plight: 'New Jersey placed between Phila. & N. York, was likened to a cask tapped at both ends; And N. Carolina, between Virga. & S. Carolina to a patient bleeding at both Arms.' Merchants and commercial bodies were at their wits' end to carry on business and petitioned for a general power over commerce.

The commercial view, as stated by Madison, was that 'the National Government should be armed with positive and compleat authority in all cases which require uniformity; such as the regulation of trade, including the right of taxing both exports & imports, the fixing the terms and forms of naturalization, &c, &c.' "

Albert J. Beveridge — *The Life of John Marshall*, Vol. I, pp. 310-312 (1916).

* * * *

"The import duties levied by the states created conflicts between the states. Some states — New York particularly — greatly lightened the burden of internal taxation by collecting substantial levies from foreign commerce. New Jersey was embittered by the fact that both New York and Pennsylvania collected import duties on goods intended for sale in New Jersey, duties which were eventually paid by the residents of New Jersey. North Carolina suffered similarly from action taken by Virginia and South Carolina. The states collected duties, not merely on goods from abroad, but on those brought in from other states as well. Virginia, with an eye particularly to the commerce of Pennsylvania and Maryland, provided for the confiscation of vessels which failed to pay duties. Restrictive laws applied to importations by land as well as by sea. Pennsylvania collected tolls on large numbers of items imported from other states. Some states enacted similar tariff measures for the combined purpose of raising revenue and giving protection to home products. If the legislation achieved these ends to some extent, it achieved also the undesirable results of interfering with the development of interstate business and of creating antagonism among the states.

* * * *

Experience with government under the Articles of Confederation demonstrated the need for certain fundamental changes if order was to be maintained and business and commercial relationships preserved and promoted. The federal government needed the power to raise revenue without the intervention of the states. In order to maintain satisfactory relations with foreign countries, it needed the power to regulate foreign commerce. In order to promote industry and commerce at home, it needed the power to levy import duties and to take over from the states the regulation of interstate commerce. It needed the power to break down and prohibit commercial barriers among the states, to deal with the national and state debts, and to prevent the forcible satisfaction of debts by depreciated paper money or by the tender of other property less acceptable to creditors than coin. It was believed that these and related measure would restore order, promote industry and commerce, and redound to the benefit of all classes of people. These considerations provide the background for the story of the adoption of the new Constitution."

Swisher, *American Constitutional Development*, pp. 25-27 (2d Ed. 1954).

* * * *

"The Constitutional Convention was called because the Articles of Confederation had not given the Federal Government any power to regulate commerce. This defect proved to be so serious that the Virginia General Assembly appointed commissioners to meet with commissioners of other states to 'take into consideration the trade of the United States; to examine the relative situation and trade of the said

states; to consider how far the uniform system in their commercial regulations may be necessary to their common interest and their permanent harmony; and to report to the several states such an act relative to this great object. . . .' Representatives of but five states met at Annapolis in September, 1786. They determined that they could do nothing by themselves, and that the adequate protection of commerce required a complete revision of the structure of government. Accordingly, they recommended that a convention be called for the purpose of revising the Articles of Confederation, and Congress thereupon asked the various states to send delegates to Philadelphia in May, 1787."

Robert L. Stern, *That Commerce Which Concerns More States Than One,* 47 Harv.L.Rev. 1335, 1337-41 (1934).

* * * *

At least three provisions of the Constitution have their roots in these problems, the Commerce Clause, the Import-Export Clause, and the Tonnage Clause. Overall, the purpose of these provisions was (1) to reserve to the United States the revenue from duties or imposts, (2) to preclude the development of a system of trade barriers at the seacoast by the States, and (3) to establish the United States as a single area of free trade without internal walls of any kind (*See Michelin Tire Corp. v. Wages,* 423 U.S. 276, 285 (1976) *reh'g denied,* 424 U.S. 935.); *see also Japan Line, Ltd. v. County of Los Angeles,* 441 U.S. 434, 449-50 (1979); *Dept. of Revenue of Wash. v. Assn. of Wash. Stevedoring Cos.,* 435 U.S. 734, 753-4 (1978).

There is an abundance of early authority applying these sections to preclude a variety of charges sought to be collected from imports, exports and interstate commerce.

In the seminal case of *Brown v. Maryland,* 25 U.S. 419 (1827) this Court, per Chief Justice Marshall, held invalid under the Import-Export Clause a Maryland Law imposing a license fee on importers. In the *Passenger Cases,* 48 U.S. (7 How.) 283 (1849), ordinances imposing a charge on every person entering the state were held invalid. In *Crandall v. Nevada,* 73 U.S. (6 Wall.) 35 (1867) the charge was on anyone entering or leaving by train. In the *State Freight Cases,* 82 U.S. (15 Wall.) 232 (1873), the charge was on freight crossing a state border. The result was the same in all of these cases: the exaction was invalidated.

Later decisions expressly found a volumetric charge based on oil flowing in interstate commerce to be invalid as an undue burden on interstate commerce. That was the conclusion reached by this Court in *Eureka Pipe Line Co. v. Hallanan,* 257 U.S. 265 (1921). There, plaintiff owned a system of pipelines in West Virginia which were connected with other lines in Ohio, Kentucky and Pennsylvania. The West Virginia two-cent throughput tax on each barrel of oil transported over plaintiff's lines was struck down. *Michigan-Wisconsin Pipe Line Co. v. Calvert,* 347 U.S. 157 (1954) *reh'g denied,* 347 U.S. 931, represented the first of many unsuccessful attempts by the State of Texas to impose a throughput tax upon the interstate export of natural gas. (*See, e.g., Calvert v. Transcontinental Gas Pipeline Corporation,* 341 S.W.2d 679 (Tex.Civ.App. 1960) and *Calvert v. Panhandle Eastern Pipe Line Co.,* 371 S.W.2d 601 (Tex.Civ.App. 1963).) The Court reached the same result as in *Eureka Pipe Line.*

We know of no modern case which is inconsistent with the result in those decisions: no case in which a simple charge by a state for the privilege of bringing merchandise in or out of a State has been upheld. But there are two other lines of authority which require discussion.

The first such line is that which deals with taxes of general application as they affect imports or interstate commerce. In *Michelin Tire, supra,* 423 U.S. 276 (1976), this Court approved the application of a general *ad valorem* property tax to imported goods. In *Washington Stevedoring, supra,* 435 U.S. 734 (1978), the Court approved application of a nondiscriminatory state income tax law. Those cases discard the old original package doctrine, looking instead, for purposes of the Import-Export Clause, at whether the tax in question is what would have been considered an "impost" or "duty" when the Clause was drafted. But *Michelin Tire* makes it absolutely clear that, if one were dealing with a simple charge for the privilege of bringing merchandise into the country, such a charge would be precisely what is prohibited. For in distinguishing an *ad valorem* property tax from imposts and duties, the Court describes such a tax as:

> *"Unlike imposts and duties, which are essentially taxes on the commercial privilege of bringing goods into a country. . ."*

> 423 U.S. at 287 (emphasis added.)

And again:

> *"The Import-Export Clause clearly prohibits state taxation based on the foreign origin of the imported goods. . ."*

> *Ibid.* (emphasis added).[4]

The opinion then goes on to point out that a foreign origin does not permit escape from uniform obligations

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[4] *Amici* rely on *Procter & Gamble Co. v. City of Chicago*, 509 F.2d 69 (7th Cir. 1975) *cert. denied*, 421 U.S. 978. *Procter* deals with a state's police power over pollution and has little or nothing to do with our problem here.

imposed on imports and non-imports alike. But all of that says plainly that a straightforward tax on goods for the privilege of entry is unconstitutional. As the concurring opinion of Justice Powell points out in *Washington Stevedoring,* a flat fee "merely for 'the privilege of moving through the State' " is bad. (435 U.S. at 764.) In the present case, the "fee" is charged simply for the privilege of crossing tide and submerged lands — *i.e.,* for the privilege of entering. We do not believe that calling the fee a "rental" changes the problem a bit.

The second line of cases requiring discussion is that of *Evansville-Vanderburgh Airport Authority District v. Delta Airlines Inc.,* 405 U.S. 707 (1972). That case involved a fee of one dollar per passenger charged by the state for the use of an airport, essentially as a way of defraying construction and operating costs. *Evansville Airport* distinguished *Crandall v. Nevada, supra,* on the ground that interstate commerce may be charged for the cost of services provided. The Evansville Airport charge was so limited; that in *Crandall* was not. In the present case, both the District Court and the Court of Appeals found that the charge has nothing to do with defrayal of costs (J.S. App. A-9, 12, 22), and, again, the finding is not contested here.[5]

It is worth noting in this connection that the old cases dealing with "tonnage taxes" draw the same line. A tonnage tax was a term applied to a charge on a ship for the privilege of tying up at a dock or anchoring in a harbor. The Constitution expressly forbids such charges. And the line drawn was that a city (a city, as a political subdivision of a state, is subject to the same rule) could charge for the use of a dock the city provided, but could

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[5]Under the "two court rule," such a finding will not be disturbed by this Court. *See Pick Mfg. Co. v. General Motors Corp.,* 299 U.S. 3, 4 (1936).

not charge for the use of an unimproved harbor or stream. Those cases are discussed infra, in part III. Thus, we have again a basic principle going back to the origins of the Constitution.

## III.

## The Market Participant Doctrine Is Inapplicable.

### A. Application of the Doctrine Would Contravene the Policy of the Commerce Clause.

The State makes no serious argument that its system of charges would be valid if considered as a tax, impost, or duty. Virtually its entire argument is directed to the proposition that the State, as a lessor, is a market participant under cases such as *Hughes v. Alexandria Scrap Corp.*, 426 U.S. 794 (1976); *Reeves, Inc. v. Stake*, 447 U.S. 429 (1980); *White v. Massachusetts Council of Constr. Employees, Inc.*, 460 U.S. 204 (1983); and *South-Central Timber Development, Inc. v. Wunnicke*, ______ U.S. ______, 104 S.Ct. 2237 (1984), and therefore, as lessor, it can charge what it wants.

The circumstances of those cases are remote from those presented here, and the doctrine totally inapplicable.

This case involves the uses of the tide and submerged lands of the states. The states did not acquire those lands as part of some enterprise into which the state entered as a voluntary market participant: on the contrary, titles to inland tide and submerged lands were acquired by the original states in their sovereign capacity as successors to the rights of the crown in England. (Later, states such as California acquired title to inland tidal and submerged inland waters upon admission to the Union.) Coastal titles were acquired pursuant to the grant made by the United States under the Submerged Lands Act.

And these rights are held, both under state and federal law, subject to special obligations toward commerce. Thus, under the Submerged Lands Act, the State's title is held subject to the paramount rights of the United States with respect to navigation. Those waters may not be obstructed without the permission of the United States, through the Secretary of Transportation or the Army Corps of Engineers. 33 U.S.C. § 401. In addition, under the California Constitution, the State's title to these lands is held in trust for fishing, recreation, navigation and commerce. Cal. Const. Art. X, §§ 3-4; *Marks v. Whitney,* 6 Cal.3d 251, 98 Cal.Rptr. 790, 491 P.2d 374 (1971); *City of Long Beach v. Mansell,* 3 Cal.3d 462, 91 Cal.Rptr. 23, 476 P.2d 423 (1970). This is not a proprietary title; it is, rather, a public purpose title.

It would be a total negation of the basis of the State's title to hold that, with respect to the lands in question, the State's position is analogous to that which it holds when it chooses to operate a cement plant (*see Reeves v. Stake, supra*). And the problem goes beyond that.

The denial by the Constitution of the power to impose imposts or duties on foreign commerce, and the equivalent prohibition implied under the Commerce Clause for interstate commerce, all existed for a powerful reason. The experience of the Articles of Confederation demonstrated the disastrous consequences of leaving in state hands the power to impose a charge merely for the privilege of entering or leaving the state. The constitutional policies created to obviate that problem are not to be casually evaded.

Liquid cargoes have to be moved either across docks or from anchorages in pipelines. If the constitutional prohibition against such charges can be circumvented merely by designating the charge as a "throughput rental" then

there is nothing left of the prohibition. Since the prohibition against such charges was and is a basic part of the effort in the Constitution to prevent the balkanization of the United States, it would hardly be sound thus to permit its evasion.

In this connection, it is most significant to note the trouble to which the Founders went to prevent such evasion. The obvious way to avoid the prohibition of imposts and duties was to place the charge on the ship rather than the cargo. Such a charge was known as a "duty of tonnage". The founders therefore included a prohibition on "duties of tonnage" as well.[6]

As we said above, it is most significant that the old cases which deal with this section draw much the same line as is drawn in the *Evansville Airport* case.

Essentially, the Clause forbids the state to levy a charge on the privilege of access by vessels to its ports. *Clyde Mallory Lines v. Alabama,* 296 U.S. 261 (1935). It has been applied to airplanes as well as to vessels because the focal point is not the vessel itself but the fact that the vessel has become an instrumentality of interstate or foreign commerce. *Scandinavian Airlines System, Inc. v. County of Los Angeles,* 56 Cal.2d 11, 14 Cal.Rptr. 25, 363 P.2d 25 (1961) *cert. denied,* 368 U.S. 899.

While most commonly applied to fees charged marine vessels for entrance to a port, the proscription against duties of tonnage applies to all fees levied against vessels or goods as a condition of access to the territorial limits of a state, regardless of how such fees are measured. *Clyde Mallory Lines, supra.*

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[6] In more detail:

> "No State shall, without the consent of Congress, lay any Duty of Tonnage . . ."

United States Constitution, Art. 1, Sec. 10, Clause 3.

Fees for access, however, are distinguished from fees for services. Fees *may* be imposed upon marine vessels or goods transported to a state's port or shore where such fees compensate the state for services and facilities "such as pilotage, towage, charges for loading and unloading cargoes, wharfage, storage and the like." (*Clyde Mallory Lines, supra,* 296 U.S. at 265.) *Quid pro quo* is the controlling principle. A state may ask compensation for services it has rendered or benefits it has foregone, but such compensation is all it may ask. Any other charge on such commerce is unconstitutional.

In *Cannon v. City of New Orleans,* 87 U.S. 577 (1874), for example, the City of New Orleans enacted an ordinance which imposed a charge on all vessels "which shall moor or land in any part of the Port of New Orleans." The Court held the ordinance was unconstitutional.

Similarly, in *Harmon v. City of Chicago,* 147 U.S. 396 (1893), the City of Chicago exacted a charge from owners of vessels operating on the Chicago River. In reversing and declaring the ordinance unconstitutional, the Court held that the charge was a tax for the use of navigable waters and not a charge by way of compensation for any specific improvement. *See also, Inman S.S. Co. v. Tinker,* 94 U.S. 238, 242-243 (1877).

The SLC has relied on *Keokuk Northern Line Packet Co. v. City of Keokuk,* 95 U.S. 80 (1877). There, the Court held valid a license fee imposed as compensation for services rendered by the City of Keokuk. But the Court was careful to point out that:

> "In nothing that we have said, do we mean to be understood as affirming that a city can, by ordinance or otherwise, charge or collect wharfage for merely entering its port, or stopping therein, *or for the use of*

*that which is not a wharf, but merely the natural and unimproved shore of a navigable river."*

95 U.S. at 88-89 (emphasis added).

It is precisely the "natural and unimproved shore" that the State wants to charge for in our case. The controlling principle is clear from these cases: a state may ask compensation only for *services rendered* to vessels bringing goods to "the territorial limits of a state . . . ", but not for the "unimproved shore." In the instant case, no assistance is rendered, nor are facilities furnished by the State to aid the lessee in transporting goods from the vessels into the state. Rather, the State provides unimproved land only, and it is the lessee who builds and maintains wharves, pipelines and other facilities for use in its operations. (J.S.App. A-9, 18.) Indeed, lessees are responsible for the removal of any such facilities upon expiration of the lease.

We point out again, this is precisely the line drawn by *Evansville Airport* for the Commerce Clause generally.

**B. The Market Participant Doctrine May Not Be Applied to Evade Constitutional Strictures.**

The *only* application of the market participant doctrine to date has been to allow the state, as the proprietor of an enterprise, the freedom to determine with whom it will deal. Thus, in the case of a state-owned cement plant or state-run scrap auto project, the state may discriminate against non-residents. *Hughes v. Alexandria Scrap Corp., supra; Reeves v. Stake, supra; see White v. Massachusetts Council of Constr. Employees, supra.* But ownership gives no blank check. In the recent case of *United Bldg. & Constr. Trades Council of Camden County and Vicinity v. Mayor and Council of the City of Camden,* ____ U.S. ____, 104 S.Ct. 1020 (1984), this Court held invalid under the Privileges and Immunities Clause a requirement that a

city contractor give preference to local residents. And in *South Central Timber Development v. Wunnicke*, ____ U.S. ____, 104 S.Ct. 2237 (1984), this Court divided evenly on the permissible inclusion in a state contract of a clause requiring the purchaser from the state of timber to cause processing to take place within the state. There is no suggestion in any opinion on the subject that "market participation" would permit a state to avoid policies which are explicit or implicit in the Constitution.

Indeed, in *Reeves* itself, this Court quoted with approval the following principle from *Alexandria Scrap:*

> ". . . The Commerce Clause responds principally to state taxes and regulatory measures impeding free private trade in the national marketplace . . . There is no indication of a constitutional plan to limit the ability of the States themselves to operate freely in the free market."

(*Id.* at 2277.)

We have already seen, however, that there is indeed a constitutional plan against the imposition of state charges for entry of goods, evidenced by at least three separate constitutional provisions and numerous decisions. That legal title does not allow escape from this plan is shown by *Foster-Fountain Packing Co. v. Haydel*, 278 U.S. 1 (1928) (which holds that state title to shrimp caught within its borders did not validate restrictions on the export of unprocessed shrimp) and *Haskell v. Cowham*, 187 F. 403 (8th Cir. 1911) (which holds that title over streets did not validate a law forbidding the construction of interstate natural gas pipelines crossing those streets). *Accord Hughes v. Oklahoma*, 441 U.S. 322 (1979) (relied on by *amici*, which reaches a similar conclusion in rejecting a state claim that it was the owner of wild minnows, and could therefore prevent their export).

## IV.

### The State's Market Participant Argument Rests on Fiction

The State argues essentially that it is merely one of a number of competitors with land available for lease; *ergo*, if an oil company is discontented, it can pick up its refinery and go somewhere else. The argument ignores the real world. Refineries are enormous complexes involving hundreds of millions of dollars in equipment. They are not on wheels. And there is essentially no coastline which does not belong either to the State of California or its political subdivisions. Appellants' map appended to their brief demonstrates that.

In addition, the State's argument (1) rests on concealment of the enormous percentage of tide and submerged lands the State owns — some 93%, (2) disregards the findings of the two courts below that the refiners "must" use State property and (3) asserts that there is private property available, when in point of fact, appellants well know that the tiny amount of privately patented tide and submerged lands cannot with any security be used for any sort of structure without an act of the legislature.

The State suggests that it is in competition with the variety of public entities to which it has granted tide and submerged land. The truth is that the public entity holdings are minuscule as compared to the State's. There are approximately three million acres of coastal tide and submerged lands. Of this, only some 200,000 acres have been placed under local jurisdiction. We quote the appellants' official publication:

> "In addition to the 49 plus million acres of land in public ownership listed in this report, there are approximately 3 million acres of coastal tide and submerged lands, of which some 200,000 acres have

been placed under local jurisdiction by legislative grant. The remainder is under the jurisdiction of the State Lands Commission."

California State Lands Commission, *Public Land Ownership in California,* p. i. (1977).

That leaves some 93% of the tide and submerged land in the State's possession.

In a constitutional sense, it makes no difference whether a particular piece of harbor shoreline or coastline is directly held by the State or has been granted by it to a city. The city, as a political subdivision of the State, is subject to the same strictures. *United Bldg. and Constr. Trades Council,* supra, 104 S.Ct. at 1026 (1984). And, in a practical sense, the budgets of city and state are today closely intertwined: the state provides funds for a wide range of local activities,[7] determines the levels of both real property and sales taxes the city may charge,[8] and dictates the conduct of its affairs in countless other ways. What goes into the pocket of one benefits the other. In its recent "bathtub conspiracy case" this Court held that parent and subsidiary corporations cannot realistically be held to be competitors. *Copperweld Corp. v. Independence Tube Corp.,* ____ U.S. ____, 104 S.Ct. 2731 (1984). In the same way, to speak of state and city as competitors in a marketplace is artificial.

Because refineries, treatment plants, and the like cannot be moved, the Court of Appeals has pointed out that

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[7]*See, e.g.*, Cal. Educ. Code § 14000, *et seq.* (state funding for local school districts); Cal. Welf. & Inst. Code § 1805 *et seq.* (state funding for local correctional programs); Cal. Water Code § 13985 *et seq.* (state funding for local clean water programs); Cal. Harb. & Nav. Code § 72.5 (state funding for small craft launching facilities); Cal. Health & Safety Code § 1100 *et seq.* (state funding for local health services programs).

[8]*See, e.g.*, Calif. Const. Art. XIIIA (Prop. 13).

the State has an effective monopoly. When lease renewals are negotiated, the dock has been built and the pipeline constructed. The refinery is already located. If, as each of the declarations shows, the State has the adjoining tidelands, (J.A. 20, 53, 60, 74, 90.) then the lease has to be obtained from the State.

Appellants attempt to meet this argument by a double-barrel speculation. They maintain, to start with, that it is not true that refineries are typically served by dedicated terminals. They make the assumption — and argue to this Court that it is a fact — that because there is a network of pipelines serving this state, that in general, oil comes in at one terminal location and is pipelined to some other refinery location. The short answer is that this argument asks the Court, on pure speculation, to upset the findings of both courts below that plaintiffs *must* use the State's land. Beyond that, this is a speculation which is inconsistent with the declarations filed, on the basis of which summary judgment was granted. Each plaintiff company has a refinery served by immediately adjacent marine terminals which are in fact a part of the refinery complex and which are essential to its functioning. (J.A. 20, 52-3, 59-60, 74, 89-90.)[9] That is not to say that there are no refineries which function in the way that the State asserts. These are refineries which are located inland, rather than adjacent to salt water, and which must receive imported crude by pipeline over land after it is brought ashore (if at all). But that is not the general rule.

Moreover, this argument is no answer at all to the underlying problem. All of the imported or interstate crude has to come ashore somewhere. For all practical purposes, all available sites are in the hands of either the State or the cities whose affairs the State controls. If the

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[9]The declarations further show that better than 95% of incoming crude is in interstate or foreign commerce. (J.A. 22, 54-5, 61, 75.)

State is successful in collecting a tariff through this sort of fee, one may be quite certain that the cities will swiftly follow. Indeed, it is the State's claim that the cities are doing it already. (Appellants' Brief, pp. 9, 26.)

The State further maintains that, because its charges are a matter of "negotiation" they are somehow validated. One might ask, if the law explicitly said that California will exact a tariff from all oil brought ashore from vessels anchored in state waters, whether the law would be validated if it went on to say "and the amount of such tariff shall be negotiated between the State Customs House and the importer." If one wishes to utilize tide or submerged lands along the coast of California, one must reach an understanding as to terms with the State or with one of the State's political instrumentalities — there is no place else to go. The State's own data confirms this. First, the map provided by the State and attached to its brief depicts in each harbor area a small encircled portion where, because the city has developed the harbor, it has been granted land by the State in trust under terms dictated by the State.[10] But even the map shows that the broad sweep of the State's title essentially goes from the Mexican border to the Oregon border. Moreover, the State's own report (cited, *supra*, at pp. 26-27) reaffirms that it directly controls some 93% of the coastline.

The State also compares its ownership to the ownership of a parcel of land in the middle of the city, and it says, quite correctly, that the owner of that land has the monopoly of that land. (Appellants' Brief, p. 21.) That is why commercial developers typically acquire fee title before erecting costly structures on downtown lots. The

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[10]Moreover, if such land turns out to be productive of large amounts of income, under California law, the State has the continuing power to reclaim it. *See Mallon v. City of Long Beach*, 44 Cal.2d 199, 282 P.2d 481, (1955).

monopoly that the State and its instruments have of the coast land and the harbors eliminates those alternatives to submitting to the landowner's monopoly power. The SLC's land cannot be sold. (Cal. Admin. Code § 2030(a)) And, by the State's own admission, lease renewals are usually only 10 years' duration (Appellants' Brief, p. 22).

There is also a suggestion in the State's brief that when a lease for a dock or a pipeline right-of-way is negotiated, the oil company will thereupon plan on amortizing the adjacent refinery over the period of the lease. This is both pure speculation and inconsistent with the real world. The major refineries both in northern California and in southern California have existed since the 1920's. Over time, as the population of the state has grown, they have been modernized and expanded; new processing units have been installed, all as the market enlarged and the technology developed. At no point is the time ever reached when it is logical for a refinery to say: at this point all of the equipment has been amortized, and our dock lease has expired, and therefore I am free to depart without loss.

The State also suggests that there are significant private landholdings which could be used to bring a pipeline to shore and they suggest that, somehow or another, by using such lands and circuitously routing pipelines, State properties could be avoided. They cite as their principal authority an article written by Assistant Attorney General N. Gregory Taylor, one of the listed counsel on appellants' brief. The article indicates that a private owner acquires only a "naked legal title"[11] and concludes that:

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[11] As the article points out, long ago, the coastline patenting of certain tidelands to private hands was once allowed.

"From this we may conclude that under *Marks*[12] *no private use of undeveloped or relatively undeveloped tidelands can be made by the private patentee of such lands with any assurance that it will not be inconsistent with the remaining public trust easement.* To proceed safely with any development the private patentee will have to obtain a legislative finding that his particular lands are no longer necessary for trust purposes."

*Taylor, Patented Tidelands: A Naked Fee?*, 47 Cal. State Bar J. 420 at 486 (1972) (emphasis added).

There is no basis on which it can be prudently assumed that any of the relatively modest amount of privately held tide and submerged land that exists here and there would be used for any of the purposes with which a refiner would be concerned without the risk that it will one day be deemed inconsistent with the public trust and will revert to the State.[13]

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[12] *Marks v. Whitney*, 6 Cal. 3d 251, 491 P.2d 374, 98 Cal.Rptr. 790(1971).

[13] In addition, the 80,000 acres the State refers to (Appellants' Brief, p. 6) is less than 2% of the total. We know of no such land at any location where it would be useful for these purposes.

## V.

## The Throughput Charge is Inherently Discriminatory Against Interstate and Foreign Commerce

It is fundamental that local legislation may not discriminate against interstate or foreign commerce. *Bacchus Imports, Ltd. v. Dias*, ____ U.S. ____, 104 S.Ct. 3049 (1984); *Hunt v. Washington State Apple Advertising Com'n*, 432 U.S. 333 (1977). It is equally fundamental that the presence or absence of discrimination is determined by the actual operation of the regulation or law. *Hunt v. Washington, supra; Nippert v. City of Richmond*, 327 U.S. 416 (1946).

There can be no question but that today, a charge on merchandise for crossing the coastline is inherently discriminatory. The reason is a simple one. In general, intrastate merchandise does not go by ship. Indeed, on the west coast, marine intrastate transportation largely ended before World War II. As to crude oil, today almost all intrastate shipment is by pipeline or by truck. (There is a limited movement of crude from the Santa Barbara-Ventura area by tanker to either Los Angeles or the San Francisco bay area to the extent that production exceeds available pipeline capacity. But that is all. And plans have been announced for the construction of a pipeline from Santa Barbara to Los Angeles, which will end most of that.) For practical purposes, the throughput charge is a tax on imports and on crude brought in from Alaska.[14] The discrimination against commerce is obvious.

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[14]The record does not develop the difference between the amounts of crude brought in, and products shipped out. In fact, we are predominantly concerned with crude shipped in. It is judicially noticeable that California is and for many years has been a crude-short area as an oil importing area. (*See, i.e.*, Bohi and Russell, *Limiting Oil Imports*, (1978) Frontispiece and p. 68). While products do move out of plaintiff's terminals, the volume is inconsequential as compared to the

The seriousness of the discrimination placed on interstate and foreign commerce is graphically demonstrated by the disproportionate rentals produced. The Clark Report commissioned by the State indicated that, at the time in question, the going rate of rental for industrial properties was 8% of its appraised value. (J.A. 339.) That 8% rental was duly provided for in the leases identified in this record. The State then went ahead and, *in addition*, collected the throughput rent with the result that the total was on the order of 20% to 28% — a fifth to over a quarter of the appraised value of the property in every year.

We would add that the basis of the "land" appraisal makes the collection even more extortionate. The State appraises tide and submerged lands on the same square footage basis as would apply to an industrial building site in the adjacent community. But this is land which, because of the public easement for commerce and navigation, and in some cases, because it is two or three hundred feet under water, cannot be used as a practical matter for anything other than the purposes which are involved here. (See, generally, J.A. 151.) One may, for instance, take the example of a tanker terminal located a mile off shore from the City of Los Angeles. There is 200 feet of water above the sea bottom. That water is swept by wind and waves of the Pacific Ocean. Yet the full sea bottom area above which tankers swing as they are anchored while loading and unloading is included in the lease. All of that property is valued as industrial property and a rental is fixed on that basis. Then, in addition, the throughput rental is tacked on as well. This is not a case when the rental collected on an appraised value is a modest rental; this is not property which has any value for any purpose

inflow. The emphasis in this brief is therefore on crude rather than products.

other than anchoring a ship. The value of the property half a mile down the coast, where there is no one who needs to anchor a ship, is probably zero.

We do not challenge the State's appraisal practices: appellees are willing to live with that problem. But to impose a tariff in addition goes too far. This is a plain and simple case of exploiting the strategic position of being adjacent to the sea in order to extract what the traffic will bear from shipping. That is precisely the sort of conduct against which the three Constitutional provisions at issue here were aimed.

## VI.

### Conclusion

The question in this case is whether the states are free to nullify the express prohibition against duties and imposts on imports by calling such a charge rent. The same question arises under the Commerce Clause's implied prohibition of the same kind of charge on interstate commerce.

Neither the State nor *amici* really address this problem: their emphasis on "proprietary interests" is no more than a pretense that the problem does not exist. As for their argument about monopoly, 93% is quite enough for a monopoly; and 98% — which is the combined acreage of the State and its political instruments — is overwhelming. What the State says is that, because of their title, any charge is permissible. We submit that the requirements of the Constitution are not so readily evaded.

Respectfully submitted,

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